Jordan's Economic Prospects and Challenges[1]
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Jordan's small, resource-poor, economy has performed well in recent years. Jordan has no oil deposits, little arable land (only 10% of the total area), and a severe shortage of water. Moreover, it has had to absorb hundreds of thousands of Palestinian, and more recently Iraqi, migrants. Despite these disadvantages and the many disruptions in the surrounding region, Jordan's economy grew at an average of 7.6% per year in 2004-07 while GDP per capita almost doubled between 1999 and 2008. Economic growth in Jordan has been broad-based and led by the manufacturing, construction, real estate, and service sectors. Growth was achieved by supplementing income from potash and phosphate exports with the emergence of the garment, pharmaceutical, tourism, and financial services industries. It also benefited from one of the world's highest levels of unilateral transfers, in the form of worker remittances and official grants. Although the external deficit widened during this period, sizeable inflows of direct foreign investment (FDI) covered three-quarters of the deficit. The remainder was officially financed by errors and omissions, which may reflect unrecorded remittances by overseas Jordanians and Iraqi immigrants. Foreign reserves increased, even though Jordan chose to retire $4.2 billion of official debt in early 2008 using proceeds from privatizations. Overall, Jordan has been an island of progress and stability in an unstable region.

Over the past ten years, the Government of Jordan (GOJ) has been very active in reforming the economy. Much of Jordan's favorable performance can be attributed to policy and administrative reforms. The public sector has continued to improve the efficiency of its expenditure and has strengthened its financial controls. Results-oriented budgeting was introduced in 2008. Meanwhile, the enabling environment for private business has improved.

Despite the elimination of fuel subsidies in February 2008, the fiscal deficit widened in 2008. Wage increases, transfer payments, and increased food subsidy payments contributed to this development. Further increases in the fiscal deficit are expected in 2009 and subsequent years.

Inflation was high in 2008 but is now moderating. Inflation soared in early 2008 as world oil and food prices spiked. Although its pace moderated late in the year, consumer prices rose by 14.9% over the year as a whole. Sharply lower world fuel and food prices since late 2008 have brought inflation down and for 2009 the expectation is that it will run at 4% or less.

Jordan's money and financial markets have remained relatively sound. Bank profitability and soundness indicators have remained favorable so far. Jordanian banks had little exposure to the mortgage-backed securities that have brought about chaos elsewhere. Nevertheless, they have been reluctant to lend. The IMF evaluated the banking system and found that it has limited exposure to interest rate, liquidity, interbank contagion, and other market risks. It is, however, vulnerable to credit and concentration risks. The IMF singled out supervision of banking groups

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as an area requiring immediate attention. Jordan's money and financial market have, however, weakened since mid-2008. The stock market has fallen since its June 2008 peak, but the decline (about 25%) has been smaller than in many other markets in the region. In October, the Central Bank of Jordan acted to maintain confidence in the banking system by guaranteeing all bank deposits until the end of 2009. It also cut interest rates (in November and again in April) and reduced reserve requirements.

Now, in common with most other world economies, Jordan faces new challenges. After growing at 5.6% in 2008, real GDP growth in 2009 is projected at 3% by the IMF, reflecting the weakness of the global and regional environments. In 2009, exports of goods and services, tourism receipts, worker remittances, and FDI are all expected to decline. Lower import quantities and prices, however, may actually bring about a narrowing of the current account deficit in the balance of payments to about 11% of GDP. Nevertheless, there are significant risks related to the financing of the external deficit. Exports, tourist receipts, remittances, FDI, and/or grant receipts could weaken more than expected if the global and regional downturns go deeper and last longer than anticipated. A sharp tightening of liquidity in the Gulf Cooperation Council (GCC) countries, which have provided a large share of FDI in recent years, may reduce capital flows into Jordan more than currently envisaged. A deeper economic slowdown in Jordan could push up unemployment, lower asset prices, and weaken the quality of banks' portfolios.

In the medium term as the world economy begins to recover, growth in the Jordanian economy should pick up once more, eventually reaching 5.5% or so. The IMF expects inflation to ease further to 2% and the current account deficit to narrow further to 9.5% of GDP, mainly through capacity expansion that will increase mining exports.

The Minister of Finance has proposed a set of far-reaching tax measures. These include cutting taxes on corporations to low, flat rate of 12%. Although mining and financial firms would pay a higher rate of 25%, this proposal would represent a major tax cut for Jordanian businesses. Tax rates for individuals would also be cut, substantially for middle-class Jordanians. Such adjustments, together with a scheme to streamline the tariff system, would make Jordan more attractive to investors but would also cause strains on the government budget. The government is also trying to encourage greater private sector involvement in public service provision, including through public-private partnerships. However, the Economic Intelligence Unit (EIU) speculates that such efforts may be stymied by the increased risk aversion of private businesses and the financial sector.

The fiscal stance in 2009 seeks to keep the deficit in check while providing some stimulus to the economy. The 2009 budget has been prepared within the framework of the on-going fiscal reforms. The GOJ is expected to react cautiously to calls for increased spending, since adding to expenditure in the absence of unexpected increases in grants or concessional loans would cause the deficit to balloon. While government's payroll may be seen as bloated, political considerations appear to rule out significant cuts.

Because of its reliance on foreign oil, the Government of Jordan (GOJ) adopted a policy of developing alternative energy sources in 2007. In addition, a natural gas pipeline from Egypt to Jordan through the southern port city of Aqaba is now operational. The pipeline has reached northern Jordan and construction to connect it to Syria and beyond is underway. Jordan developed a new energy strategy in 2007 that aims to develop more indigenous and renewable energy sources, including oil shale, nuclear energy, wind, and solar power.

Job creation is a major challenge. Unemployment in 2008 was officially reported to be 13% of the labor force. Unofficial estimates run as high as 30%.

Yet a young, relatively well educated, population is a potential asset for Jordan's future economic development. Thirty-eight percent of the population is below the age of 14. Education and literacy rates and indicators of social well-being are relatively high compared to other countries with similar income levels. Population growth, previously high, has dropped to 2.2%. Life expectancy is 71 years for men and 74 years for women. The population is highly urbanized (estimated at 80%). King Abdullah II's long-term vision for Jordan sees this population profile as a demographic asset that can be used to transform the country into a modern knowledge-based economy. The long-term vision involves modernization of the country's economic, institutional, and political infrastructure, based on the enhancement of its human capital, and the elimination of poverty. Education, improving the business environment, and attacking poverty are at the core of this vision.

Jordan's business enabling environment is relatively favorable and has improved in recent years, but further improvements are needed to help advance private sector development. Jordan ranks 101st out of 181 countries and territories in the World Bank's Doing Business Indicators for 2009. However, it ranked only 131st in starting a business (which reportedly involves ten procedures and takes 14 days), 128th in enforcing contracts, 123rd in getting credit, 115th in registering property, and 113th in protecting investors. Areas in which Jordan ranked higher are closing a business (93rd), dealing with construction permits and trading across borders (74th), employing workers (53rd), and paying taxes (22nd).

Jordan has received strong donor support. The World Bank reports having lent Jordan $2.4 billion through 2008. World Bank Group assistance focuses on improving the investment environment, promoting public-private partnerships, and providing better financial packages for projects in water and energy. The International Finance Corporation has made direct investments. USAID, a major donor, works to increase the competitiveness of Jordan's private sector, attract more investors, and create more jobs and higher incomes. One of its principal emphases is institution building for trade facilitation. USAID's activities include efforts to spread the benefits of development by reaching small businesses and improving the social safety net. USAID supports the development of the Aqaba Special Economic Zone, which is regarded as a model framework for private sector development. In October 2006 the Millennium Challenge Corporation (MCC) signed a Threshold Program Agreement with the GOJ in support of reform efforts in municipal governance and customs administration. In November 2006 Jordan was selected as one of the countries eligible for additional MCC assistance; the GOJ has since begun the process of applying for MCC Compact Assistance.

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